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CITATIONS

In the Supreme Court of the United States

OCTOBER TERM, 1961

No. 493

J. L. ENOCHS, DISTRICT DIRECTOR OF INTERNAL REVENUE, PETITIONER

v.

WILLIAMS PACKING & NAVIGATION CO., INC.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the District Court (R. 272–284) is reported at 176 F. Supp. 168. The opinion of the Court of Appeals (R. 285–298) is reported at 291 F. 2d 402.

JURISDICTION

The judgment of the Court of Appeals was entered on June 14, 1961. (R. 298.) By order of the Chief Justice, dated September 11, 1961, the time for filing a petition for a writ of certiorari was extended to October 12, 1961. The petition was filed on that date and was granted on December 11, 1961. (R. 299.) The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED

Whether, under this Court's decision in *Miller* v. *Nut Margarine Co.*, 284 U.S. 498, the district court had jurisdiction to entertain a suit to restrain the collection of taxes allegedly erroneously assessed, despite the prohibition of Section 7421(a) of the Internal Revenue Code of 1954.

STATUTE INVOLVED

Internal Revenue Code of 1954 (26 U.S.C.):

> SEC. 7421. PROHIBITION OF SUITS TO RESTRAIN ASSESSMENT OR COLLECTION.
>
> (a) *Tax.*—Except as provided in sections 6212 (a) and (c), and 6213(a), no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court.
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> * * * * *

STATEMENT

A. THE INITIATION OF THE PRESENT PROCEEDINGS

This case originated upon the filing of a complaint (R. 1–6) by the Williams Packing & Navigation Company, Inc. (hereinafter referred to as the taxpayer) for an injunction to restrain the District Director of Internal Revenue, Mississippi, from collecting social security and unemployment taxes in the total amount of $41,568.57, which had been assessed against it for taxable periods during the years 1953, 1954, and 1955. The assessments resulted from the determination of the Commissioner of Internal Revenue that the Captains and crewmen

who performed services as fishermen aboard trawlers owned or leased by the taxpayer were employees of the taxpayer within the meaning of the term "employee" as defined in Sections 1426 and 1607 of the Internal Revenue Code of 1939 and the corresponding provisions (Sections 3121 and 3306) of the Internal Revenue Code of 1954. (R. 272–273.) The taxpayer's complaint (R. 1–4) alleged that it was engaged in a "joint venture" with the fishermen and that no employer-employee relationship was involved.

Pursuant to the taxpayer's motion and after a hearing at which the court heard and considered oral and documentary evidence, the District Court granted a preliminary injunction. (R. 6–7.) The court made no finding that the District Director's assessment was arbitrary, capricious, or otherwise "illegal."

B. THE EVIDENCE PRODUCED AT TRIAL

The trial of taxpayer's suit to restrain the collection of assessed taxes involved the receipt of the oral testimony of eighteen witnesses, the depositions of three others, and a large number of exhibits. It produced a trial transcript of over 600 pages. The facts and evidence produced at trial may be summarized as follows.

1. *Williams Packing & Navigation Co. and DeJean Packing Co.*

Taxpayer is a Louisiana corporation, organized in June, 1944, and qualified to do business in Mississippi, with its principal place of business at Biloxi, Mississippi. Its incorporators were Elmer Williams, president (19 shares); his brother, Carroll Williams, Jr.,

secretary-treasurer (19 shares); and Lucius Frieberger (2 shares). It was organized to engage in the seafood packing business; to own, operate, lease, manage, and control boats, machinery, appliances, and tackle for fishing for, dredging, and catching oysters, shrimp, crabs, and other species of fish. (R. 272–274.)

The DeJean Packing Company (hereinafter referred to as DeJean), a partnership doing business in Biloxi, Mississippi, is closely allied to taxpayer. Its members are the aforementioned Williams brothers and their respective wives. Formed in 1943 as the successor to DeJean Packing Company, Inc., a Mississippi corporation dissolved in the same year, DeJean was founded to carry on its predecessor's business of acquiring, processing, and marketing sea food, including shrimp, oysters, and certain other species of fish. (R. 31–33.) DeJean owned, operated, and controlled a group of buildings used for processing sea food. Taxpayer, with no separate telephone or post office box of its own, used these buildings and facilities as well as the business office of DeJean. (R. 44–45, 48–52, 215.)

The dominant and key figure of both taxpayer and DeJean was Elmer Williams, who spent most of his working day in and about the aforementioned premises and supervised most of the business operations of both entities. (R. 78, 89, 274.) Williams instructed Leon Hall, his son-in-law, in the operation of the plant. (R. 10–11, 23.) For his judgment "in a lot of things", particularly the financial condition and banking position of both companies, Williams depended

upon Lucius Frieberger, office manager of DeJean and a director, stockholder, and secretary of the taxpayer. Frieberger, paid by DeJean, kept the books of both DeJean and the taxpayer. (R. 54–55, 87–89, 274.)

2. Taxpayer's methods of operation

Elmer Williams, who knew of the fishermen along the coast of Mississippi, including the capable and competent ones to whom he safely could entrust the boats which the taxpayer owned or leased, would let a boat to a captain of his selection for particular trips or for the fishing season. Upon taking possession of the boat, the captain would take the requisite papers to the office of the Bureau of Customs for the necessary statutory endorsement thereon. (R. 34, 36–37, 182, 205–206, 275–276.) The captain would hire the crew (usually two for shrimping and four for dredging oysters) and would procure the necessary fuel, groceries, and ice for the fishing trip, which might last from ten days to two weeks. The fuel would usually be purchased at the DeJean docks from that company's fuel facility. (R. 34–35, 77, 124, 172, 182–183, 221, 254, 276.) Ice would be obtained from the Biloxi Freezing Company, a corporation of which Elmer Williams was vice-president and a stockholder. Groceries would be purchased at a store owned by Leon Hall (DeJean's production manager and Elmer Williams' son-in-law). Other equipment would be obtained from the DeJean trawl shop. The items purchased would be initially charged to the taxpayer and later deducted from the gross price allowed for a catch. (R. 35, 41, 64–66, 174, 221–222, 264, 276.)

When a catch was brought in to the DeJean docks and sold to DeJean, it would be unloaded on a conveyor system, weighed, and thereafter processed by DeJean. A record of the catch would be made and given to the captain, who would then take it to Frieberger. Frieberger, acting for the taxpayer, would compute the value of the catch at prices which the taxpayer fixed (evidenced by price lists issued to the boat captains from time to time); deduct therefrom the expenses of the trip (fuel, groceries, ice, etc.); and divide the remainder into shares—one share each to the captain and each member of the crew, one share to the taxpayer for use of the boat (the boat share), and another to the taxpayer for the rig (nets, equipment), until the latter was paid for. A check would be made payable to the captain, who, in turn, would make distribution to the crew. This method of compensation was known as the share, or "lay", system.[1] (R. 41, 90–91, 163, 277; Deft. Ex. 18, R. 239–240.)

3. *The financial relationship between the taxpayer and DeJean*

The taxpayer invoiced DeJean at the end of each month for the total amount of the product delivered. The transaction was recorded on the taxpayer's books as a sale to DeJean. DeJean's books reflected a cor-

[1] On occasions a trip resulted in a "broker", i.e., no catch, in which event the unpaid costs of the trip were carried forward and deducted from the catch of a succeeding trip. In the event of a "broker" the taxpayer advanced money to the fishermen out of its general funds. When a captain and crew members left the taxpayer's service, the taxpayer absorbed the loss attributable to advances or extensions of credit. (R. 41–42, 70, 74–75, 277–278.)

responding purchase from, and a liability to, the taxpayer. From time to time (as determined by Frieberger), DeJean issued checks to the taxpayer in varying sums, also determined by Frieberger, which did not necessarily reflect the full amount of any invoice. Frieberger admitted that it was within the scope of his employment to determine how much money should be paid to the taxpayer. (R. 90–92, 115–116.)

The taxpayer and DeJean both operated on the same fiscal year basis. At the end of each such year and after audit, the taxpayer negotiated with DeJean a so-called "handling charge", or "profit", for itself (R. 106), the amount of which Elmer Williams and Frieberger determined (R. 68–69; and see Deft. Ex. 14, R. 233–237). The "handling charge" per the monthly invoice was one-half cent per can for oysters; it varied from $1 to $1.50 per barrel for shrimp. (Deft. Ex. 14, Schedule B–2, R. 235). Following the close of each fiscal year the "handling charge" or "profit" was usually arbitrarily increased—retroactively for each barrel of shrimp and can of oysters—when the taxpayer's boat expenses exceeded its income from boat shares. (Deft. Ex. 14, R. 235; R. 106.)

4. *Taxpayer's financial condition*

The taxpayer consistently lost money on its sales of fish to DeJean from the fiscal year ending in June 1952 to that ending in June 1958. (Deft. Ex. 14, Schedule A, Line 3, R. 233.) However, the monthly and annual receipts in the name of "handling

charges" resulted in an overall profit for the fiscal years through 1955. As of June 30, 1955, and, in so far as the record shows, as of the date on which the taxpayer learned of the assessments here involved, taxpayer had an accumulated surplus slightly in excess of $50,000. (Deft. Ex. 14, Schedule A, Line 8, R. 233.)

At the conclusion of fiscal 1956, after the taxpayer had received notice of the tax here in issue (R. 231–232), the taxpayer's practice underwent the following change. For fiscal 1956, the taxpayer incurred a loss from boat operations in the amount of $50,529.89. The handling charge it received per monthly invoices was only $13,337.484. (Deft. Ex. 14, Schedule A, Lines 3–4, R. 233.) No year-end increase was made in the handling charge (Deft. Ex. 14, Schedule B–2, par. 1, Line 2, R. 235), and the taxpayer accordingly incurred a net loss for the year in the amount of $37,615.58 which decreased its accumulated surplus to $16,373.09 (Deft. Ex. 14, Schedule A, Lines 7–8, R. 233). No year-end adjustment increasing the handling charge was made for fiscal 1957, during which period the expenses from boat operations exceeded the taxpayer's income from boat shares and the monthly invoice handling charges. (Deft. Ex. 14, Schedules A, B–2, R. 233–235.) There was a resultant elimination of the taxpayer's surplus and the creation of a deficit in the amount of $328.56. (Deft. Ex. 14, Schedule A, Line 8, R. 233.)[1]

[1] On July 23, 1957, taxpayer sold to DeJean for their $19,580.66 book value two trawlers the value of which was estimated to be $50,000. (R. 198–200, 218.)

More significant than the existence or absence of corporate surplus or of a substantial net worth of the taxpayer is evidence of the taxpayer's capacity to raise enough money to forestall a levy upon its assets and financial ruin. In this regard, taxpayer was not necessarily faced with a requirement of paying the entire assessment of $41,568.57 plus interest, or facing bankruptcy and liquidation. There is nothing to show that he attempted to pay the assessment for one taxable period[3] while requesting deferral of collection for the other taxable periods involved until the legal issues could be litigated in a refund proceeding. It defies credulity to believe that the taxpayer, which was owed $20,269.02 by the DeJean partnership (R. 151), could not have obtained $2,000 from the partnership to pay the assessment due for one quarter.[4]

5. The evidence on the question of employee status of the fishermen

The issue of liability for social security and unemployment taxes in this case depends upon whether the captains and crews of respondent's fishing boats were its "employees" within the meaning of Sections 1426 and 1607 of the Internal Revenue Code of 1939 and of Sections 3121 and 3306 of the 1954 Code. Each of these sections specifically incorporates common law rules for determining status as an employee.

(a) The government relied upon the following evidence to justify an inference of an employer-employee status.

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[3] See *Flora* v. *United States*, 362 U.S. 145, 171, n. 37; *Steele* v. *United States*, 280 F. 2d 89 (C.A. 8).

[4] The assessments, by taxable quarters, are set out at page 5 of the printed record.

(i) The relationship between the respondent and the crews of the ships was not, in general, sporadic or of short duration. Several captains testified that they had plied the same trade, using respondent's vessels for 35, 20, and 15 years. (R. 156, 223–224, 263.)

(ii) Taxpayer maintained substantial power to control the activities of its crews. It could and would lease its ships to whom it pleased. (R. 34, 36–37.) There was evidence that respondent could control the quantity of ice taken on any trip and thus could control the duration of the trip. (R. 221, 264.) Taxpayer, as almost exclusive purchasing agent for each crew's catch, could control the type of fish sought. (R. 33, 37, 222–223, 244, 266.)

(iii) There was evidence that respondent intended to and on occasion did exercise its power of control over the ships' crews. Each leased ship almost invariably purchased its groceries, on credit, at a store owned by Leon Hall, the son-in-law of the president and principal stockholder of respondent. (R. 35, 64–65, 165–166, 181–182, 222, 245–246, 264.) The testimony of respondent's president strongly suggests that a captain's failure to buy from Leon Hall would be a relevant factor in consideration of whether he should be retained in respondent's fleet. (R. 65–66.) Fuel and ice were regularly purchased from respondent or a closely related seller, although there was testimony that at least the fuel could be obtained more cheaply elsewhere. (R. 76, 221, 254.) There was evidence that respondent would contact those of its ships which were radio-equipped and direct them either to return

or not to return to port on a particular day, depending upon the then current supply of shrimp on hand at the DeJean plant. (R. 58, 219, 221.) Other evidence of actual exercise of control was the testimony that the men had to obtain permission to sell their catch to anyone other than the taxpayer; that the men needed permission to go out in the boats when DeJean had no need of more fish; that the taxpayer sometimes dictated the nature of the catch; and that the price paid for the catch was in general unilaterally determined by respondent. (R. 163, 222–223, 238–240, 266.)

(iv) Finally, the parties themselves had at times described their relationship as that of an employer to an employee. During World War II taxpayer or DeJean or Elmer Williams applied for and obtained draft deferments for captains and crew members by representing that these men were employees. (R. 231.) On separate occasions two captains filled out "Master's Certificates of Service" for admission to the United States Marine Hospital at New Orleans. Each certificate indicated that the captain regarded himself as an employee. (Deft. Exs. 3, 8(a).) DeJean represented to the Federal Public Housing Authority that some of the fishermen were employees entitled to wages at specified rates. (Deft. Ex. 5, pp. 1–12.)

(b) The taxpayer, on the other hand, produced evidence that the captains were free to buy their provisions where they wished; that the captains hired and controlled their crews; that the captains chose their fishing grounds and methods; and that the crews

were not compelled to sell their catch exclusively to taxpayer and DeJean.

C. THE DECISIONS OF THE DISTRICT COURT AND OF THE COURT OF APPEALS

The district court found that the captains' regular purchase of supplies from the taxpayer or related sellers was due to the convenience, efficiency, and services of the sellers and not because of any "control, right of control or coercion" on the part of the taxpayer. (R. 276–277.) It found that the taxpayer neither exercised nor retained a power to control the methods of fishing and that the captains were free to sell their catch wherever they pleased. (R. 277.) The trial judge concluded that there was no employer-employee relationship between the taxpayer and the captains and crews of the ships involved. Upon the basis of this conclusion and its finding that (R. 279):

> * * * if the levy had been made upon the assets of the corporation it would have wrecked the corporation and thrown it into bankruptcy, as it did not have and does not have assets with which to pay the taxes and not sufficient assets with which it could have negotiated a loan to pay the tax.

the court granted a permanent injunction restraining the collection of the contested unemployment and social security taxes. (R. 284.) The District Court did not find that the assessment was arbitrary and capricious; nor was there any record evidence to support such a finding.

The Court of Appeals affirmed. (R. 293.) Judge Rives, dissented (R. 293–298). He noted that the

holding of the majority was in direct conflict with the decision of the Eighth Circuit in *Kaus* v. *Huston*, 120 F. 2d 183, and that the rationale of *Miller* v. *Nut Margarine Co.*, 284 U.S. 498 (R. 296), "cannot be extended to bring within some supposedly implied exception cases like the present one without emasculating the prohibition" of Section 7421 of the 1954 Code against injunctions restraining the collection of taxes.

SUMMARY OF ARGUMENT

Section 7421(a) of the Internal Revenue Code of 1954 states, in clear and unmistakable terms, that "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." The twofold purpose of this prohibition—institution of a uniform system for judicial determination of the correctness of a tax assessment and protection of the government's paramount need of being able to collect its revenues without dependence upon a prior judicial adjudication—has been recognized by this Court in a number of cases for over a hundred years. Where Congress has been willing to allow an exception to the provisions of Section 7421(a), as in the case of Tax Court proceedings, it has expressly incorporated the exception into the statute.

In *Miller* v. *Nut Margarine Co.*, 284 U.S. 498, this Court, dealing with a unique factual situation which involved an assessment characterized by the Court as arbitrary and capricious, engrafted a narrow exception upon the broad and clear prohibition of the statute. The *Nut Margarine* exception requires the

existence of two factors: (1) an illegal exaction (p. 509) "in the guise of a tax," and (2) the presence of "special and extraordinary circumstances sufficient to bring the case within some acknowledged head of equity jurisprudence."

The requirement of an illegal exaction in the guise of a tax cannot be satisfied by a mere allegation or showing of a bona fide mistake of law or fact. If it could, Section 7421(a) would be of no force and effect and its purpose of requiring payment prior to resort to a uniform system of judicial determination of liability would be frustrated. This Court and the court of appeals have held that an assertion or showing of simple error of law or fact does not make a tax assessment "illegal" in the sense required to be enjoinable.

In the present case neither court below purported to find any illegality in the assessment of tax beyond their determination on the merits that the taxpayer was not in fact liable for the taxes asserted. Moreover the court did not make and, indeed, the record would not support a finding of an arbitrary or capricious assessment. Since one of the two requirements necessary to bring the taxpayer within the *Nut Margarine* exception to Section 7421(a) was not satisfied, a suit to restrain the tax assessments could not properly be entertained and the judgment below must be reversed.

ARGUMENT

A. SECTION 7421(A) EXPLICITLY PROHIBITS SUITS TO ENJOIN THE ASSESSMENT OR COLLECTION OF ANY TAX

The single question presented is whether, under the facts and circumstances of this case, the district court

had jurisdiction to enjoin the collection of the social security and unemployment taxes involved, in light of the statutory prohibition contained in Section 7421(a) of the Internal Revenue Code of 1954, *supra*, p. 2.

That section states, in the clearest possible terms, that "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." The provision has been federal law, in substantially identical form, since 1867.[1] It reflects a Congressional determination that the complexities of administering the revenue laws necessitate a uniform system for the review of asserted tax liabilities and that, in light of the government's paramount need promptly to secure its revenue, the proper remedy for contesting an assessment or collection is

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[1] Section 10 of the Act of March 2, 1867, 14 Stat. 471, amended Section 19 of the Act of July 13, 1866, 14 Stat. 98, by the addition of the phrase "And no suit for the purpose of restraining the assessment or collection of tax shall be maintained in any court." Section 19 set forth the conditions under which suits might be maintained for the refund of taxes alleged to have been erroneously assessed. In the Revised Statutes the phrase added in 1867 was modified slightly and became Section 3224: "No suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." Section 3653(a) of the 1939 Code and Section 7421(a) of the 1954 Code are identical, except for the addition of provisions relating to cases pending before the Tax Court, not germane here. Cf. 28 U.S.C. 1341, whereby Congress has also prohibited restraint by the federal courts of the assessment or collection of any tax under state law where there is an adequate remedy at law in the state courts. For comment on the paucity of the legislative history of Section 3224, see Gorovitz, *Federal Tax Injunctions and the Standard Nut Cases*, 10 The Tax Magazine 446 (1932), and Note, 49 Harv. L. Rev. 109 (1935).

an action for recovery of the payment of the tax. (See *Allen* v. *Regents*, 304 U.S. 439, 456 (concurring opinion), rehearing denied, 304 U.S. 590; *Bull* v. *United States*, 295 U.S. 247, 259-60; *State Railroad Tax Cases*, 92 U.S. 575; *Phillips* v. *Commissioner*, 283 U.S. 589, 596; *Flora* v. *United States*, 362 U.S. 145.)

As early as 1875, this Court in *Cheatham* v. *United States*, 92 U.S. 85, 89, clearly recognized the prohibition against enjoining the assessment or collection of a tax as an essential governmental safeguard:

> If there existed in the courts, State or National, any general power of impeding or controlling the collection of taxes; or relieving the hardship incident to taxation, the very existence of the government might be placed in the power of a hostile judiciary. • • • While a free course of remonstrance and appeal is allowed within the departments before the money is finally exacted, the general government has wisely made the payment of the tax claimed, whether of customs or of internal revenue, a condition precedent to a resort to the courts by the party against whom the tax is assessed. • • •

To the extent that Congress deemed it necessary to limit the general prohibition against enjoining the assessment or collection of any tax, it provided an express statutory exception to the clear command of Section 7421(a). By its own terms, that section is inapplicable where the Commissioner has determined a deficiency of income, estate, or gift taxes (under Section 6212 (a) and (c) of the 1954 Code), the taxpayer has filed a timely petition for redetermination of such deficiency (as provided in Section

6213(a)[6]) and that petition is pending before the Tax Court. In such situations, no assessment or collection of tax is to be made until a final determination is rendered by the Tax Court, and Section 6213(a) explicitly provides that the making of an assessment or levy prior thereto may be enjoined.[7] Thus, with respect to income, estate, and gift taxes, Congress has explicitly created a special statutory right to judicial determination of liability prior to payment.

In sharp contrast, Congress has made no exception to the government's right to collect social security and unemployment taxes before issues of liability with respect thereto are adjudicated. The provisions relating to those taxes—here involved—have been incorporated in Subtitle C of the 1954 Code,[8] and are not covered by the exception of Section 6213(a). See *Enochs* v. *Green*, 270 F. 2d 558 (C.A. 5th). Section 7421(a) applies with full force, therefore, to bar any "suit for the purpose of restraining the assessment or collection" of the taxes in the instant case.

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[6] Section 6213(a) provides in pertinent part:

"* * * no assessment of a deficiency in respect of any tax imposed by subtitle A or B and no levy or proceeding in court for its collection shall be made, begun, or prosecuted until such [90-day] notice has been mailed to the taxpayer * * *. Notwithstanding the provisions of section 7421(a), the making of such assessment or the beginning of such proceeding or levy during the time such prohibition is in force may be enjoined by a proceeding in the proper court."

[7] However, where the Secretary of the Treasury or his delegates believe that the assessment or collection of a deficiency will be jeopardized by delay, Section 6861 commends that he shall immediately assess and collect the tax, notwithstanding the provisions of Section 6213(a).

[8] See Sections 3101 and 3301 of the 1954 Code.

B. MILLER V. NUT MARGARINE CO., 284 U.S. 498, RECOGNIZED A NARROWLY LIMITED EXCEPTION FOR INJUNCTIVE ACTIONS WHEN A COURT IS PRESENTED WITH BOTH EXTRAORDINARY CIRCUMSTANCES AND AN ILLEGAL EXACTION IN THE GUISE OF A TAX

In addition to the statutory exception of Sections 6212 and 6213, this Court has engrafted a judicial exception to the plain words of Section 7421(a). In *Miller* v. *Nut Margarine Co.*, 284 U.S. 498, this Court was presented with the following facts. The taxpayer sought an injunction restraining the Collector from collecting any tax under the Oleomargarine Act.[9] Three prior district court adjudications had declared identical products to be nontaxable, and a Treasury Decision had been published to the same effect. Most important, the taxpayer had been advised by letter from the Collector that its product would not be taxed. Also, the Collector had acquiesced in other injunction proceedings contesting similar attempts to impose tax, and had made no effort to tax other identical products being marketed. Relying upon all of the foregoing, the company commenced manufacture and sale. About eighteen months thereafter, the Collector (p. 505) "demanded and threatened to collect" a tax of 10¢ per pound upon the product. If required to pay the tax, the company's loss would have amounted to 7¢ per pound; furthermore, the company had already sold so much of its product that payment of the tax would have destroyed its enterprise.

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[9] Act of August 2, 1886, 24 Stat. 209, as amended by Act of May 9, 1902, 32 Stat. 193.

In these circumstances, this Court found (pp. 510–511) that the Collector's determination of tax liability was "arbitrary and capricious" (p. 508); that a "valid oleomargarine tax could by no legal possibility have been assessed"; and the discrimination shown conflicted "with the principle underlying the constitutional provision directing that excises laid by Congress shall be uniform throughout the United States"; and that it required "no elaboration of the facts found to show that the enforcement of the Act against respondent would be arbitrary and oppressive."

On these facts, which the Seventh Circuit has described as manifesting "administrative caprice," [10] this Court held that the statutory prohibition against suits to restrain an assessment or collection was subject to judicial modification where two requirements are met (p. 509): (1) there is a showing of "the illegality of an exaction in the guise of a tax"; and (2) there are present "special and extraordinary circumstances sufficient to bring the case within some acknowledged head of equity jurisprudence, * * *." [11]

C. THE REQUIREMENT OF "AN ILLEGAL EXACTION IN THE GUISE OF A TAX" CANNOT BE SATISFIED BY A MERE ALLEGATION OR SHOWING OF A BONA FIDE MISTAKE OF LAW OR FACT

The boundaries of an "illegal exaction" sufficient, if accompanied by extraordinary circumstances, to over-

[10] *Homan Mfg. Co.* v. *Long*, 242 F. 2d 645, 653.

[11] Justices Stone and Brandeis dissented on the ground that the statute precluded injunctive relief "whatever the equities alleged."

come the prohibition of Section 7421(a) are not susceptible of precise definition. It is, however, entirely clear that if the statutory prohibition is to have any effective content the requirement of illegality can not be satisfied by a mere showing of an error of law or fact. Questions of the correctness of the assessment or collection of any tax are the intended routine fare of the statutory system for the review of tax liabilities. The very purpose of the enactment of Section 7421(a) was to assure the uniform operation of the provisions requiring payment and then a civil action for a refund under Section 7422 to contest tax liability. If, on a request for injunction, the assessment or collection of a tax could be scrutinized on its merits on the ground that an erroneous assessment is an "illegal exaction," then the government would in every case be required to await the determination of judicial proceedings to collect the tax it asserts is due, and there would be no case in which the taxpayer is made to rely upon the uniform statutory procedure for contesting the validity of a tax assessment. In short, Section 7421(a) would be of no force and effect, for the remaining requirement of hardship making the remedy at law inadequate would add nothing to the general requirements of equity jurisdiction.

This Court and the courts of appeals have always recognized that far more must be shown than the error of a tax assessment if the prohibition of Section 7421(a) or its predecessors are to be avoided. Dealing with R.S. 3224, a predecessor of Section 7421(a), this Court, in *Snyder* v. *Marks*, 109 U.S. 189, 192, described a "tax" as—

> * * * that which is in a condition to be collected as a tax, and is claimed by the proper public officers to be a tax, *although on the other side it is alleged to have been erroneously or illegally assessed.* * * * [Emphasis supplied.]

See also *Dodge* v. *Osborn,* 240 U.S. 118; *Phillips* v. *Commissioner, supra.* In the *Nut Margarine* case, where injunctive relief was granted, the Court spoke of "arbitrary and oppressive" enforcement, of an "arbitrary and capricious" determination, of a tax which "could by no legal possibility have been assessed," and of "discrimination" on the part of the Collector. All these terms are descriptive of administrative determinations for which no legal basis exists—determinations which on their face are in violation of law. The very words—"arbitrary," "capricious," "discrimination"—have definite legal connotation and suggest results reached through administrative action which itself exceeds administrative power, rather than, simply erroneous results reached by the administrator while working within the proper limitations of his role.

In *Kaus* v. *Huston,* 120 F. 2d 183, a case closely analogous on its facts to this, where the taxpayer contended that social security and unemployment taxes could not be legally assessed against him because he was merely the lessor of taxicabs to independent operators rather than the employer of the drivers, the Eighth Circuit denied injunctive relief, stating (120 F. 2d at 185):

> It is true that where a complainant demonstrates that what purports to be a tax is merely

an exaction in the guise of a tax and that there are special and extraordinary circumstances which bring the case under some acknowledged head of equity jurisprudence, a suit may be maintained to enjoin the collection of the pseudo-tax. *Miller* v. *Standard Nut Margarine Co.*, 284 U.S. 498, 509, 52 S. Ct. 260, 76 L. Ed. 422. The validity of the taxing act under which the assessments against appellant were made has been sustained. * * * The assessments are for taxes, and not for exactions in the guise of taxes. The appellant may not owe them, but that does not change their nature, nor is nonliability a special or extraordinary circumstance. This case presents the ordinary situation of a taxpayer resisting payment of taxes which he believes that he does not owe.[12] * * *

D. SINCE THERE WAS NO SHOWING OF AN "ILLEGAL EXACTION" AND NEITHER COURT BELOW FOUND MORE THAN AN ERRONEOUS ASSESSMENT OF A TAX, SECTION 7421(a) OF THE INTERNAL REVENUE CODE OF 1954 DEPRIVED THE COURTS BELOW OF JURISDICTION TO ENJOIN THE ASSESSMENT OR COLLECTION OF THE TAXES IN ISSUE

There is no doubt that in the present case an erroneous standard was applied to the "illegality" requirement of the *Nut Margarine* case in allowing the restraint of the collection. Both the district court and the court of appeals granted the injunction on the ground that, under the facts of the case, the Com-

[12] See also *Missouri Valley Intercol. Ath. Ass'n.* v. *Bookwalter*, 276 F. 2d 365 (C.A. 8); *Mensik* v. *Long*, 261 F. 2d 45 (C.A. 7); and *Homan Mfg. Co.* v. *Long*, 242 F. 2d 645 (C.A. 7).

missioner had incorrectly asserted the existence of tax liability. There was no finding of administrative caprice, nor of an arbitrary or discriminatory assertion of tax liability where none could possibly exist. Nor was there any doubt expressed concerning the good faith of the taxing officials or as to the procedural regularity of the administrative action taken.

The District Judge clearly stated why he found the asserted liability to be "illegal" (R. 280):

> I find as a fact that the relationship of employer and employee as defined by the Social Security Act did not exist and does not exist between the corporation and the captains of the boats and the crewmen, and that the tax was illegally and unlawfully levied, * * *

He summarized, "If the relationship of employer-employee did not exist, then the levy was unlawful"—*i.e.*, the levy could be enjoined. (R. 273.)

The opinion of the Court of Appeals, in affirming the grant of the injunction, also plainly indicates that the requisite "illegal action" was grounded on nothing more than the court's determination that, under the facts of the case, the Commissioner had made an erroneous assessment. Judge Cameron, speaking for the majority, stated (R. 286–287) that "* * * the question underlying disposition of the whole case, that is, whether the fishermen were employees of the taxpayer corporation, was one essentially to be resolved from the facts as developed from the large number of witnesses the court heard." Likewise, Judge Rives, dissenting, described the issue deemed controlling by the majority as "closely and

hotly litigated purely as a question of fact." (R. 297.)

It is equally certain that there was no basis in the record for a finding of an abuse of the District Director's administrative powers. The evidence produced before the trial judge and summarized in the Statement (*supra*, pp. 10–12) makes clear that the District Director could reasonably find and conclude: (1) that the taxpayer retained as much control of the fishermen's activities as was practical considering the necessity of substantial independence of a ship at sea; (2) that the taxpayer exercised or would have exercised this control whenever necessary to assure that supplies were purchased from it or related sellers, that the catch was sold only to it, and that only fish which taxpayer or DeJean could use were caught; and (3) that this much control of persons who regularly used taxpayer's equipment over long periods of time to furnish a service necessary to taxpayer's business indicated that the fishermen were in fact taxpayer's employees. Indeed in another series of cases involving an analogous fishing operation the captains and crew members were found to be employees after a jury trial.[13] If these conclusions would have been warranted on the record before the district court, it cannot be asserted that the Commissioner's assessments, based on similar con-

[13] *R. E. Clegg* v. *United States*, Nos. 456, 457, decided January 10, 1962 (S.D. Tex.); *Johnson R. Clegg* v. *United States*, No. 458, decided January 10, 1962 (S.D. Tex.); *Clegg Shrimp Co.* v. *United States*, No. 459, decided January 10, 1962 (S.D. Tex.).

clusions from similar evidence, were even unreasonable, much less arbitrary or capricious."[14]

Since the record will not sustain a determination that the District Director's assessments represented an abuse of his administrative powers and since no such determination was in fact made by the courts below, the present case does not satisfy one of the two requirements of the *Nut Margarine* case—that the assessment must constitute not merely error but an illegal exaction "in the guise of a tax". Not having brought itself within the *Nut Margarine* exception to Section 7421(a), taxpayer is properly subject to the clear prohibition of that section that "no suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." Both courts below were without jurisdiction to entertain the taxpayer's suit and the judgment below must be reversed.

E. THE GRANTING OF A PRELIMINARY AND A PERMANENT INJUNCTION AGAINST THE ASSESSMENT OR COLLECTION OF TAXES WHERE ONLY A POSSIBLE ERROR IN THE ASSESSMENT IS ALLEGED OR SHOWN UNDERMINES THE PURPOSES OF SECTION 7421(a)

The judicial proceedings in the present case were initiated with the filing of a complaint in the district court more than four and one-half years ago. A preliminary injunction was issued immediately there-

[14] Prior to making the assessments, the Internal Revenue Service had interrogated numerous captains and crew members who worked aboard taxpayer's boats and had examined taxpayer's books and records (R. 231–232). Thereafter, the Internal Revenue Service reconsidered and upheld the assessments in connection with taxpayer's claims for abatement (R. 5).

after and was lifted only when it was replaced by a permanent injunction. Even if the government had won its case in the district court, it would have been delayed almost two years in the collection of its revenue by the preliminary injunction. If in that circumstance a stay had been granted pending appeal or if the government had first won its case on the merits in the appellate court, the government would have been delayed three and three-quarters years in the collection of revenue.

Congress has deliberately considered the question as to which party should bear the inevitable delays of judicial determination of tax liability. It has chosen between the risks of requiring the taxpayer to rely on the government's administrative assessment of tax liability pending judicial determination and the risks of requiring the government to rely on the judgment of district courts acting on application for preliminary injunction pending final judicial determination of tax liability. For almost one hundred years it has placed the burden of delay upon the taxpayer in unequivocal terms. The power of Congress to make this determination and to have it fully respected by the federal courts continues to be an essential implement of Congress' broader power to assure the nation's fiscal responsibility.

The *Nut Margarine* exception to the plain wording of Section 7421(a) and its predecessors is consistent with the purposes of the statute only so long as it continues to require a tax which "could by no legal possibility have been assessed" and an administrative determination which is manifestly "arbitrary and capricious"—in sum, so long as what is enjoined can

fairly be said to be not what would ordinarily be called a tax assessment or tax collection but a flagrant abuse of administrative powers which is merely labeled "tax collection" for purposes of deception.

Finally, this substantive standard will not in itself guarantee that Section 7421(a) will have its intended effect unless it is applied sympathetically at the earliest possible stages of proceedings, particularly in the district court's action on an application for a preliminary injunction. Even if the district court had applied the proper standards of Section 7421(a) after a complete trial in the present case, the government would have been subjected to an unnecessary and fruitless trial and would have been delayed almost two years in the collection of a tax assessment which Congress has determined the government may collect and use pending judicial resolution of any *bona fide* disputes as to liability.

CONCLUSION

For the reasons stated, it is respectfully submitted that the judgment below should be reversed, and the case remanded with instructions to dismiss the complaint.

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